



On June 21, 2018, the Supreme Court issued its highly anticipated opinion in [\*Lucia v. SEC\*](#), finding that the manner in which the U.S. Securities and Exchange Commission (SEC) selects its "in-house" administrative law judges (ALJs) violates the Appointments Clause of the Constitution.



In a 7-2 decision, the Court held that ALJs are "inferior officers" and must be appointed by the president or head of the agency, rather than hired by SEC staff through the civil service process. The immediate practical impact of the decision requires that petitioner Raymond Lucia be afforded a new hearing before "a properly appointed official." In recent years, capitalizing on what some commentators considered a "[home court advantage](#)" for enforcement actions, the SEC began [favoring](#) administrative proceedings in which agency ALJs serve as adjudicators rather than judicial proceedings in federal court. An ALJ assigned to hear an SEC enforcement action has the power to issue an initial decision containing factual findings, legal conclusions, and appropriate remedies. The Commission is not required to review the ALJ's decision, and if it declines to review, the ALJ's "initial" decision is deemed a final action of the Commission. In practice, most ALJ initial decisions become final without any Commission review; for example, [2016 data revealed that 90% of SEC ALJ initial decisions](#) were not reviewed by the Commission. ***Circuit Split*** In 2012, an SEC ALJ imposed sanctions amounting to \$300,000 in civil penalties and a lifetime bar from the investment industry on Lucia for his acts in violation of the Investment Advisers Act. Lucia appealed to the D.C. Circuit, arguing that the SEC's administrative proceeding was invalid due to the fact that the agency's ALJs were unconstitutionally selected by SEC staff. Lucia argued that ALJs are "Officers of the United States" and are therefore subject to the Appointments Clause of the Constitution, which requires appointment by the president, a court of law, or the head of an agency. Lucia lost his appeal before the D.C. Circuit, but a decision reached by the Tenth Circuit in a [separate case](#) found that SEC ALJs are "inferior officers" empowered with "significant discretion" and thus subject to the Appointments Clause. The Supreme Court resolved this circuit split, reversing the D.C. Circuit and finding for Lucia. Justice Kagan authored the opinion and relied primarily on the Court's analysis in [Freytag v. Commissioner](#), which found that the United States Tax Court's special trial judges were "inferior officers," because they exercised "significant discretion" when carrying out "important functions." The Court reasoned that SEC ALJs similarly wield "significant authority" given that they preside at hearings, issue opinions, and decide sanctions for those charged with violating securities laws. Because SEC ALJs act as more than "mere employees," they must be appointed pursuant to Article II, Section 2, Clause 2 of the U.S. Constitution. ***Practical Impact*** The SEC, as well as a litany of current and past respondents in SEC administrative proceedings, will now work to interpret and apply the Court's narrow holding in *Lucia*. The Court made particular note of the fact that Lucia is entitled to relief due to his "timely" challenge to the constitutional validity of the appointment of the ALJ who adjudicated his case, consistent with the Court's holding in [Ryder v. United States](#)—a note which may foretell the Court's position on whether historic SEC adjudications are eligible for re-hearing. Additionally, on November 30, 2017, the SEC [issued an order](#) "ratifying" the prior appointments of its ALJs in an effort to "put to rest any claim that administrative proceedings pending before, or presided over by" SEC ALJs violate the Appointments Clause. Although Lucia argued that the Commission's ratification order was invalid, the Court declined to address that argument and ruled only that a different ALJ must hear Lucia's case in the new hearing. Lastly, while the SEC has a total of five ALJs, the federal government [employs almost 2,000 ALJs in more than 30 agencies](#), many of which could be impacted by the Court's holding in *Lucia*.

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